

**CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM  
STATEMENT OF INVESTMENT POLICY**

**FOR  
RISK MANAGEMENT PROGRAM**

**February 14, 2005**

*This Policy is effective immediately upon adoption and supersedes all previous Risk Management Program policies.*

**I. PURPOSE**

This document sets forth the investment policy, guidelines and procedures ("the Policy") for determining the strategic and tactical management of investment risk for the California Public Employees' Retirement System ("the System") through the Risk Management Program ("the Program"). The Policy allows for sufficient flexibility to capture investment opportunities as they may occur, yet establishes reasonable risk parameters to ensure prudence and care in the management of the System's assets.

**II. STRATEGIC OBJECTIVE**

The Program shall be managed to accomplish the following:

- A. Enable the System's investment program to achieve one of its primary strategic objectives: the highest return possible within *prudent* levels of risk and liquidity.
- B. Enhance the effectiveness of the CalPERS investment portfolio to provide CalPERS with a reasonable balance between risk and return.
- C. Provide an integrated process for overall risk management on both a consolidated and disaggregated basis.
- D. Provide effective tools to aid the investment decision making process by providing value added decision making support.
- E. Enable the maintenance of a positive working relationship with the investment operation.
- F. Promote a risk management culture within CalPERS through education and example.

### III. RESPONSIBILITIES AND DELEGATIONS

- A. The CalPERS Risk Management Program, headed by the Senior Investment Officer - Risk Management, shall facilitate the management of the economic and investment risks of the System. It is not intended to manage other risks that the System faces, including but not limited to, Operational Risks, Compliance Risks and Legal Risks, which are managed by CalPERS Legal office, including the Enterprise-wide Compliance function and is covered by their own sets of policies and procedures. The program is not intended to uncover fraud.
- B. The System's Investment Committee ("the Investment Committee") is responsible for approving and amending this Policy. The Investment Committee delegates the responsibility for administering the Risk Management Program to the System's Investment Staff.
- C. The Asset Allocation and Risk Management Unit has responsibilities that include, but are not limited, to the following:
  - 1. The development and modifications of, and recommendations regarding this Policy to the Investment Committee.
  - 2. The implementation and adherence to this Policy.
  - 3. The selection, development, maintenance and enhancement of the risk management tools used by the Program to provide analyses that support the investment actions of the entire CalPERS Investment Staff.
  - 4. The reporting on the System's investment risks and associated returns to the Investment Committee and Investment Staff. See Section V.
  - 5. The education on risk management concepts, and the uses of and benefits from risk management in the investment process to ensure a risk-aware culture at CalPERS.
  - 6. The supply of forward looking risk management analyses to be used to manage the CalPERS investment program.

- D. The Risk Management Consultant and General Pension Consultant are responsible for advising staff on risk management efforts and reporting to the Investment Committee as appropriate.

#### **IV. TOTAL PROGRAM BENCHMARKS**

The Program shall be benchmarked against the risk management practices of other major pension fund peers to remain in the forefront of and to achieve the “best practices” of pension fund risk management. There is no specific industry-wide benchmark standard. Each investment asset class and program within the asset class has its own benchmark.

#### **V. MONITORING AND REPORTING**

- A. Staff shall provide monthly reporting on the investment risks of the CalPERS portfolio. These reports are to provide the expected volatility or risk and Value at Risk (“VAR”) of the CalPERS invested and policy portfolios. These analyses are to show risks for the entire investment program, for each separate asset class, for groups of accounts and for individual accounts and managers. The analyses shall provide ex post results and ex ante forecasts of absolute levels of risk and risks relative to benchmarks at all levels of the investment program. The monitoring and reporting shall enable the investment staff to manage the CalPERS investment program through the achievement of the strategic objectives stated in Section II of the Policy document.

##### **1. Monitoring**

- a. Identify and manage the risk levels of the CalPERS investment portfolios, and ensure that CalPERS understands and is properly rewarded for the risks it assumes.
- b. Identify fund diversification and investment risks that arise from the implementation of the System’s Asset Allocation Policy to identify, minimize or eliminate uncompensated risks.

##### **2. Reporting**

The reporting package shall include, but is not limited to:

- a. Asset Allocation reports providing an analysis of the System’s current asset allocation relative to the System’s policy asset allocation to be used by Senior

Investment Staff in their monthly Asset Allocation Meeting.

- b. Total Portfolio reports showing the current level of risk being taken with a comparison the history of the risks that have been taken.
  - c. A Concentration report to highlight the 20 companies in which CalPERS has greatest concentration of investment across asset classes and portfolios.
  - d. External Manager Monitoring reports for the purpose of monitoring the System's external managers.
  - e. Customized reports and analyses for the asset class investment units as needed.
  - f. Reports to evaluate the accuracy of the risk management system forecasts and the efficiency of the investment risks taken by the System.
- B. The Risk Management Program shall be continuously reviewed to enhance the timeliness, accuracy and usability of the Program's risk management tools through improvements in systemization and automation.
- C. The Chief Investment Officer, Senior Investment Officers and their professional investment staffs shall incorporate the ex ante and ex post information, analyses and results of the Risk Management Program into the investment decision making process.

## **VI. GLOSSARY OF TERMS**

The Miscellaneous Glossary of Terms is referenced in the System's Master Glossary of Terms.